INCA
Portfolio Managers

Annexure E

HESSEQUA MUNICIPALITY

Long Term Financial Plan – *Update 2016*

Prepared by
INCA Portfolio Managers
November 2016

REPORT OVERVIEW – INTRODUCTION AND BACKGROUND

The Hessequa Municipality appointed INCA Portfolio Managers in 2013 to prepare a Long Term Financial Plan. The report was entitled ***Hessequa Local Municipality Long Term Financial Plan: 2014 – 2023***; October 2013 (referred to as the 2013 Estimate). The report was updated in November 2014 and February 2016 (referred to as the 2014 and 2015 Estimates respectively) with the then latest available information. This November 2016 Update (2016 Estimate) aims to review the conclusions reached previously based on the latest available information and report on the findings.

The **objective of the Plan** is to recommend strategies and policies that will maximise the probability of the municipality's financial sustainability into the future. This is achieved by predicting future cash flows and affordable capital expenditure based on the municipality's historic performance and the environment in which it operates.

A summary of the demographic-, economic- and household infrastructure perspective was updated with the latest available information as published by iHS Global Insight. The historic financial analysis was updated with the information captured in the municipality's ***unaudited*** financial statements of 30 June 2016. INCA Portfolio Managers' Capital Investment Model was populated and run with this latest information, and the outcome thereof is reported herein. In particular the capital budget assumptions and funding mix assumed by the municipality for the 3 years from 2016/17 to 2018/19 were accommodated in the revision of the model.

Unlike the original assignment, no renewed analysis of the Asset Register, review of municipal documents (viz. IDP, Master Plans, etc.) and conversations with management were undertaken. The conclusions reached in this report are complimentary to the recommendations made previously.

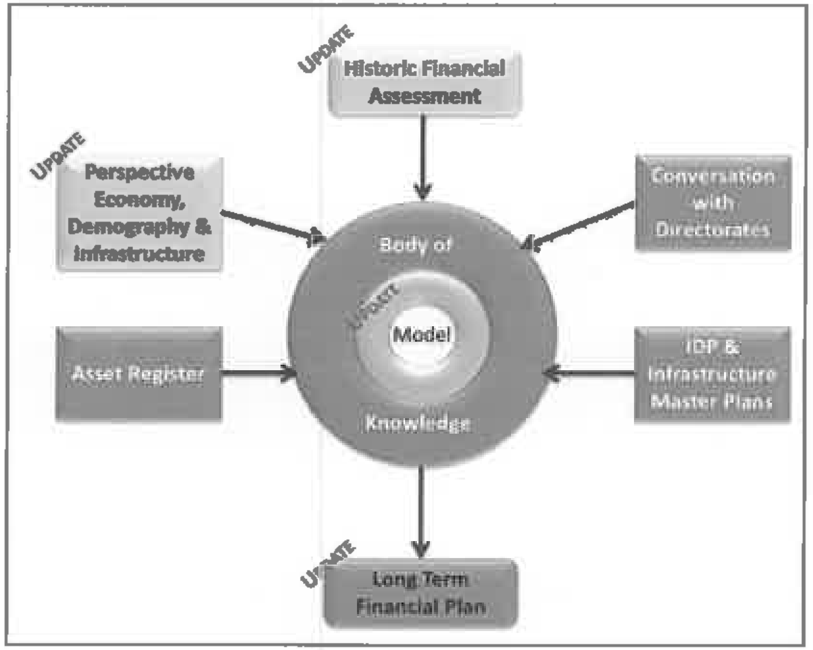
The contents of this report entail the following:

1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	Ratio Analysis
8	Conclusions

1	**Planning Process**
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	Ratio Analysis
8	Conclusions

PROCESS

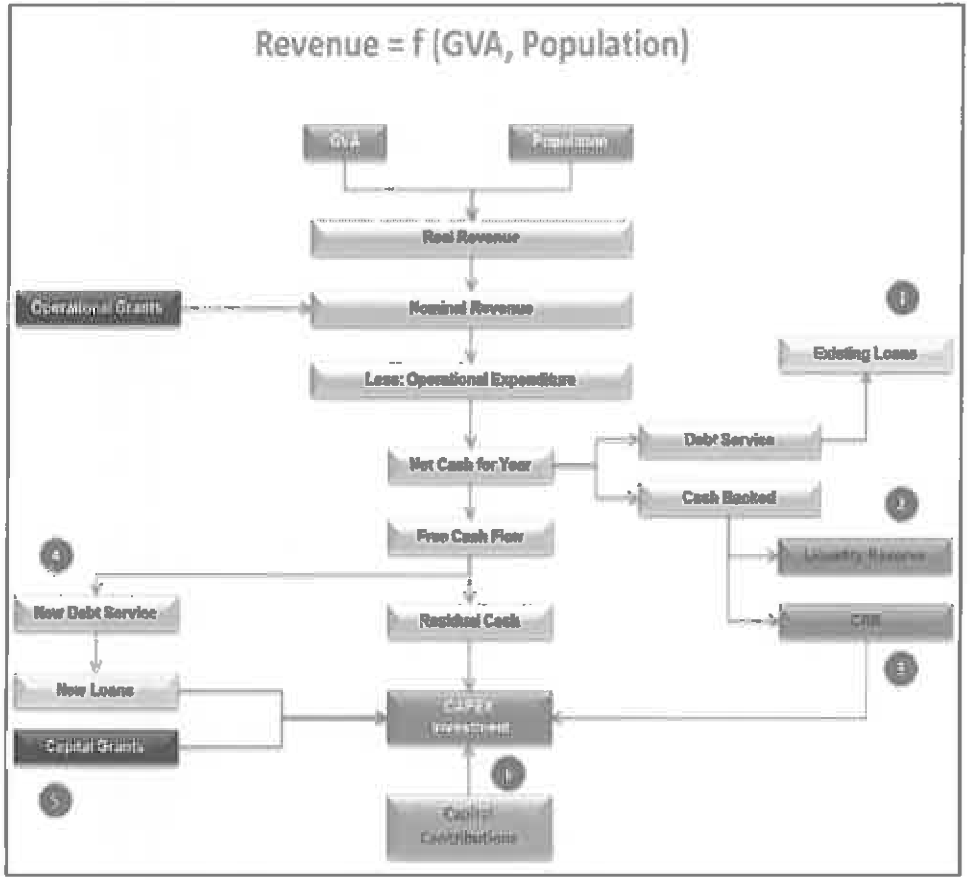
The diagram below illustrates the steps in the process that were followed in 2013 and the steps updated in 2014 and 2016:



The diagram below illustrates the process followed to determine the affordable future capital expenditure. Future projected municipal revenues are estimated by applying the relationship:

Revenue = f (Economy (i.e. GVA[1]), Population)

The cash available for capital investments is then determined by deducting operational expenditure, debt service amounts as well as liquidity- and capital replacement requirements from the projected revenue.

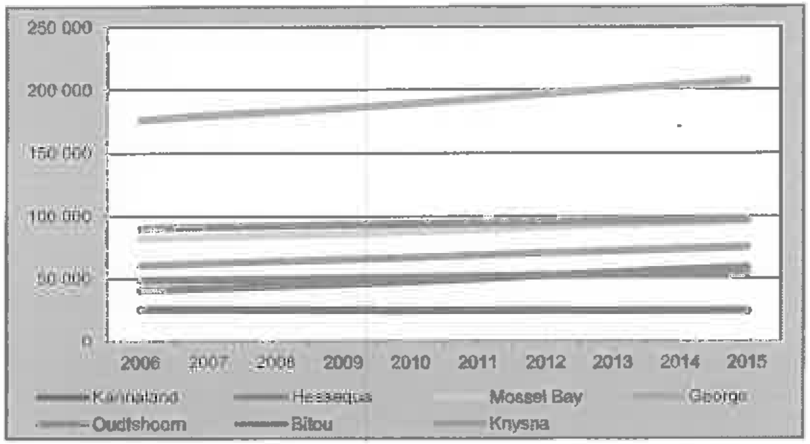


[1] GVA = Gross Value Add

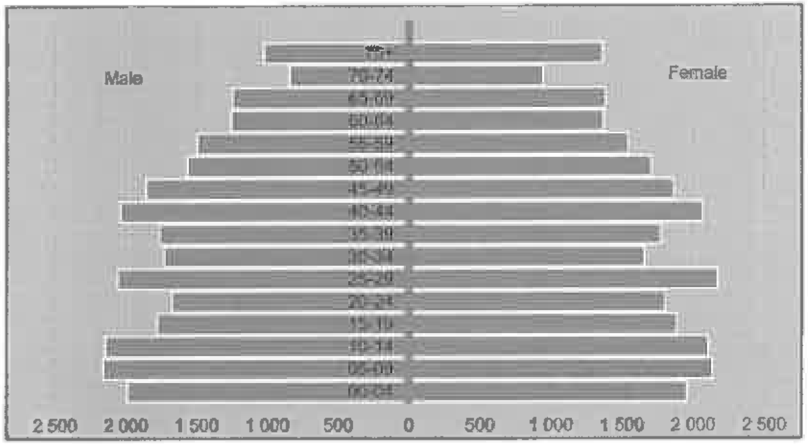
1	Planning Process
2	**Updated Perspectives (Demographic, Economic, Household Infrastructure)**
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	Ratio Analysis
8	Conclusions

DEMOGRAPHY

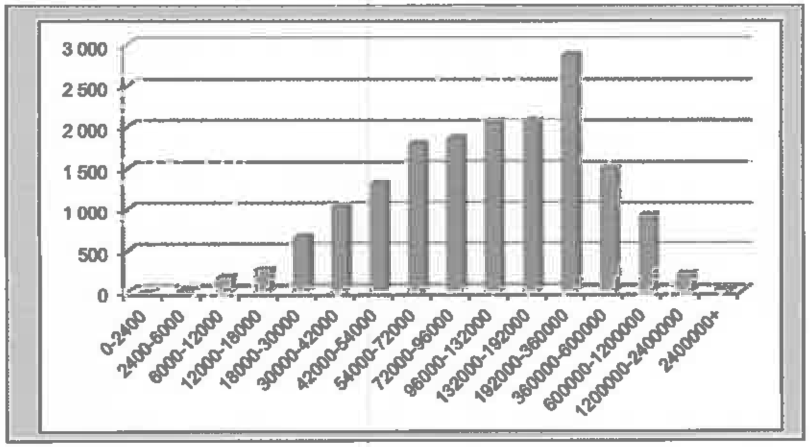
The ***Population*** reflected in Hessequa's IDP (3rd review) is 48 500, 12% undercounting to the current estimated population of 54 356 (2016). Hessequa currently has the third lowest population growth rate (1.3%) of the seven municipalities in the District and is lower than the Western Cape (1.7%) and National growth rate (1.5%).



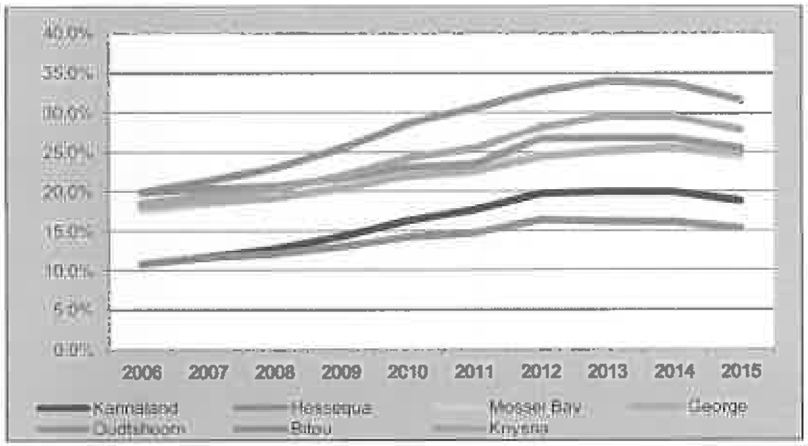
Unlike the classical pyramid, the ***Age Profile*** illustrates that there are proportionally fewer people in the age group younger than 40 years, indicative of a mature population.



The ***Household Income*** distribution illustrates that the proportion of household earning less than R 30 000 p.a. constitute approx. 11%.

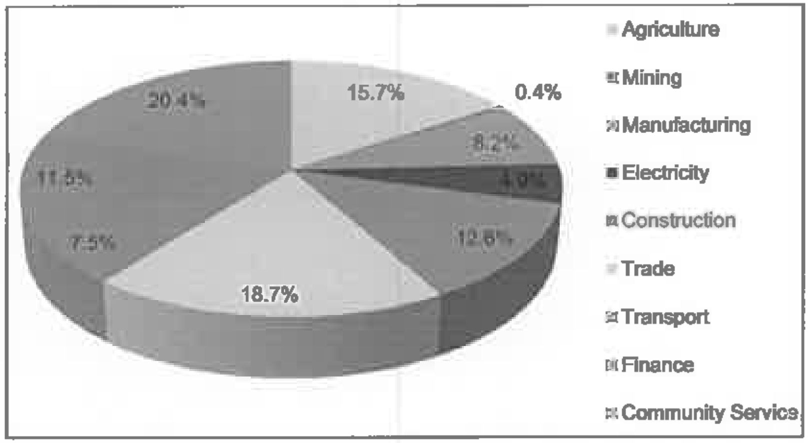


The ***Unemployment Rate*** for 2015 is the lowest of the seven municipalities in the District at 15.3%, and much lower than the Western Cape and National unemployment rate of 21.8% and 25.5% respectively

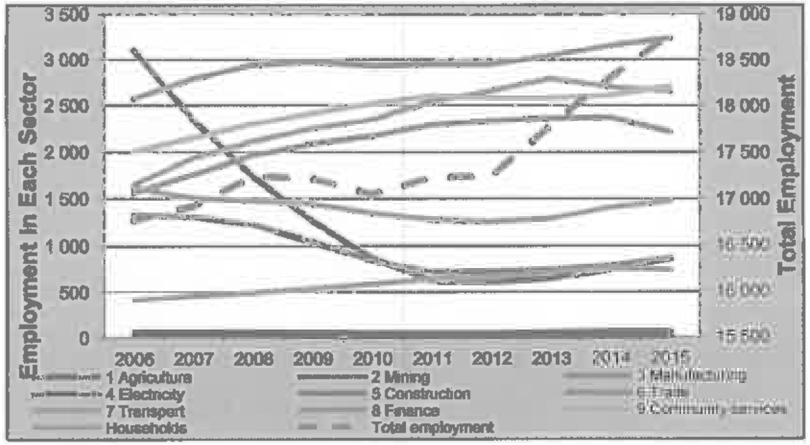


ECONOMY

Community Service remains the dominant ***Economic Sector*** with 20.4% of the output in 2015, followed by Trade (18.7%) and Agriculture (15.7%).



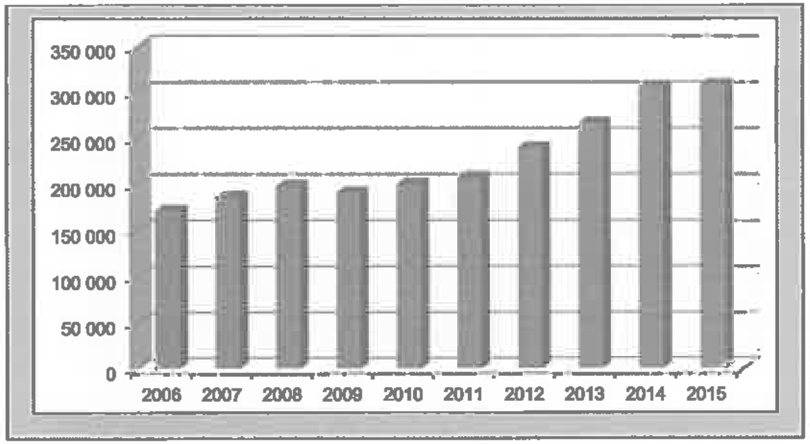
The Trade sector is the largest Employer at 17.3% of total employment; furthermore, the employment in this sector reflects an increasing trend since 2010. Community services and Finance are also significant employers, contributing 14.4% and 14.2% to employment respectively. Whereas employment in Agriculture has declined during the first half of the past decade, it now appears to have stabilised.



Proportional growth was experienced in the Electricity, Construction and Trade Sectors, with all other sectors experiencing stagnant or a decline in growth from 2006 to 2015. Although Transport showed a decline from 2006 to 2015, it has shown a small steady increase since 2010 (7.1%).

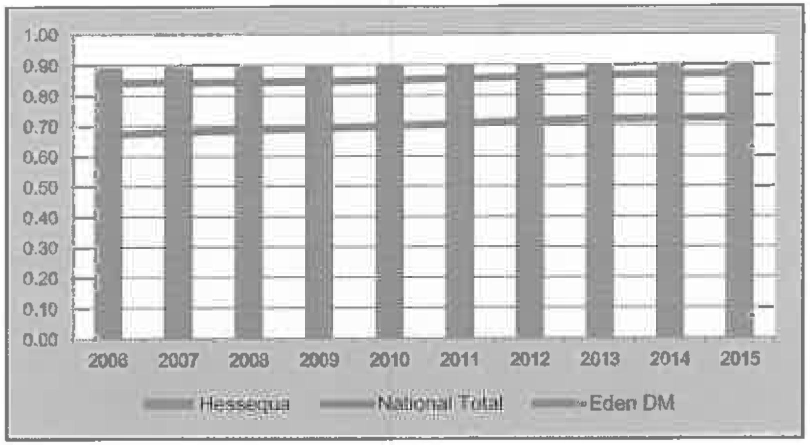
Sector	2006	2015
1 Agriculture	17.7%	15.7%
2 Mining	0.4%	0.4%
3 Manufacturing	9.1%	8.2%
4 Electricity	2.5%	4.9%
5 Construction	9.1%	12.6%
6 Trade	16.7%	18.7%
7 Transport	8.8%	7.5%
8 Finance	14.1%	11.5%
9 Community services	21.5%	20.4%

Tourism Spend amounted to 10.2% of GVA, a slight decrease when compared to 10.6% of 2014.

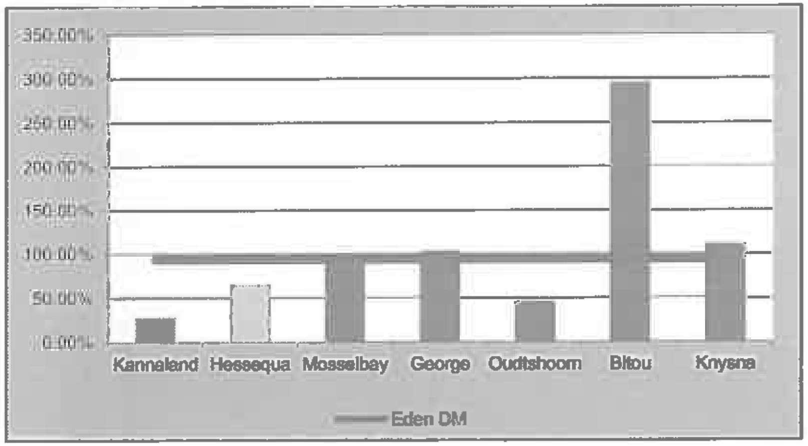


HOUSEHOLD INFRASTRUCTURE

The ***Infrastructure Index*** is a high 0.91 which given the high percentage of indigent households could imply that the high level of service may become unaffordable in future.



Growth in ***Household Formation*** between 1996 and 2015 was 63%, the third lowest of all seven municipalities in the district. However in absolute numbers, the growth of households in Hessequa of 6 526 was the second lowest during this period.



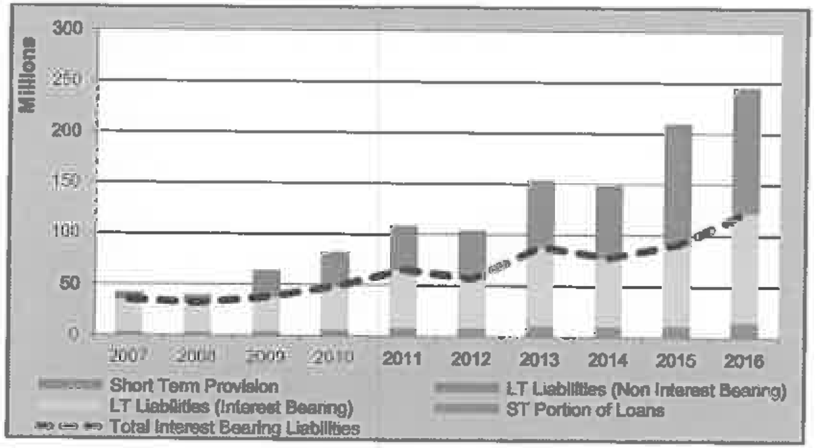
By comparing backlogs of ***sanitation, water, electricity and refuse removal*** in urban as well as non-urban areas, Hessequa Municipality performed better with regards to sanitation and electricity and worse with regards to water and refuse removal than the average of all the municipalities in the Eden District.

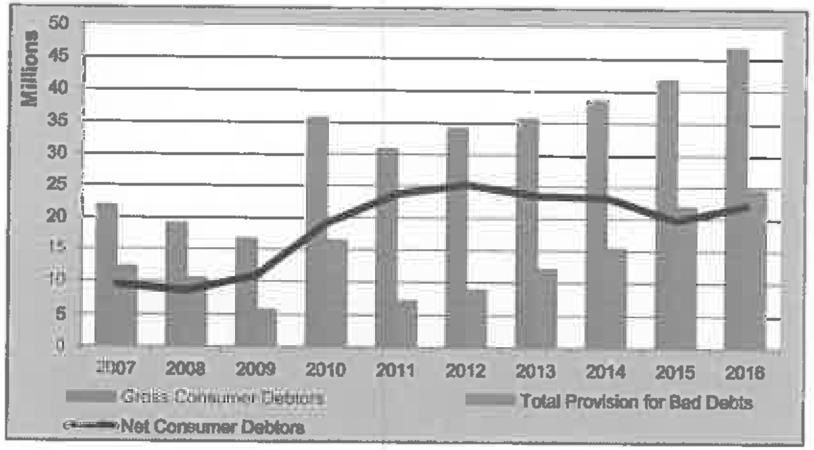
Infrastructure	Eden DM	%	Hessequa	%
Above RDP Level				
Sanitation	159 226	89.1%	15 620	93.0%
Water	169 485	94.9%	15 670	93.3%
Electricity	166 736	93.3%	16 348	97.3%
Refuse Removal	159 743	89.4%	14 058	83.7%
Below RDP Level or None				
Sanitation	19 397	10.9%	1 183	7.0%
Water	9 137	5.1%	1 133	6.7%
Electricity	11 886	6.7%	455	2.7%
Refuse Removal	18 880	10.6%	2 745	16.3%
Total No. of Households	178 622	100.0%	16 803	100.0%

1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	**Updated Historic Financial Assessment**
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	Ratio Analysis
8	Conclusions

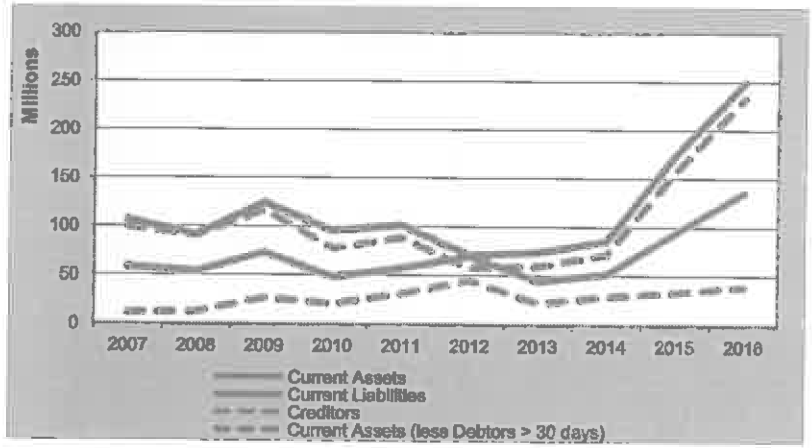
Financial Position

Total Liabilities continued to increase since FYE2014. The increase was mainly due to a 35% increase in ***Interest Bearing Liabilities*** from R 90.45 m to R 121.96 m in FYE2016, pursuant to a net increase in new loans of R 31.46 m. ***Non-Interest Bearing Liabilities*** continues its increasing trend and amounted to R 123.43 m in FYE2016. The movement was mostly influenced by the 5% growth in ***Non-current Provisions.***





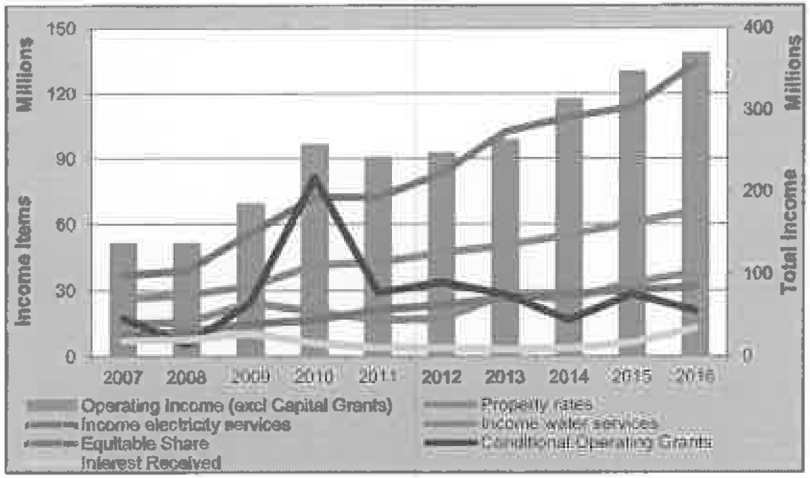
Liquidity Ratio remained positive and improved substantially since FYE2012 to 1.84:1 in FYE2016, mainly due to Cash and Cash Equivalent increasing by R 70.09 m (51%) to R 206.79 m as at FYE 2016. **Current Assets** grew by R 74.98 m (43%) and **Current Liabilities** grew by R 41.17 m (44%) during the period. Cash and Cash Equivalents constituted 83% of Current Assets



Gross ***Consumer Debtors*** continues its increasing trend since FYE2011 and averaged a growth rate of 9% annually in the last five years. The municipality reported a ***Collection rate*** of 97%. Bad debts written off on rates and service debtors amounted to R 1.86 m in FYE2016.

The allowance for doubtful debts amounts to 117% (FYE2015: 100%) of outstanding **debtors older than 90 days**, and has increased by R 5.33 m (28%) to R 24.57 m in FYE2016.

INCOME AND EXPENDITURE

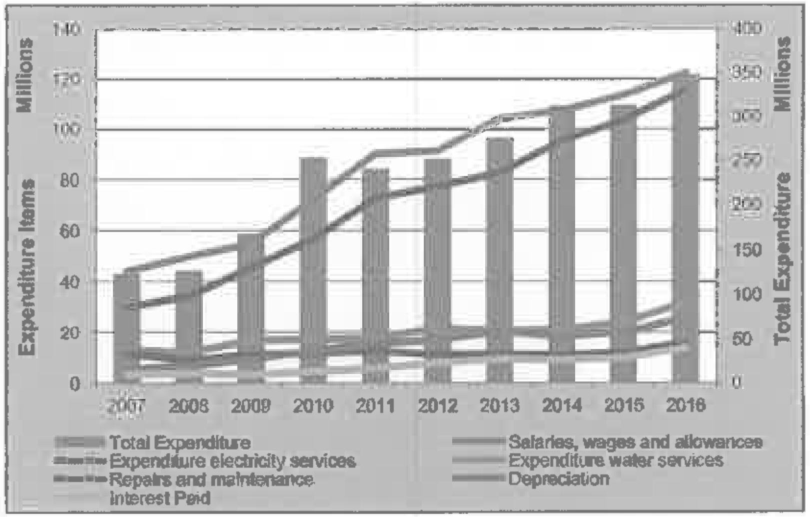


Total Operating Income (excluding Capital Grants) increased by R 22.49 m (6%) to R 369.39 m in FYE2016, from the prior year.

The main revenue generating items remained the same proportionally, dominated by sales of **_Electricity Services_** contributing 36%, **_Property Rates_** (18%), **_Water Services_** (10%) and **_Equitable Share_** (9%).

Interest earned (on external investment) accelerated by 107% to R 12.64 m as at 30 June 2016. Gain on revaluation of Investment Property decreased by R 9.19 m to R 0.71 m in FYE2016.

Important to note is that the revenue and expenditure from **_Water_** and **_Electricity Services_** are derived from Segmented Income Statement for the year ended 30 June 2016 but not from the Statement of Financial Performance.



Total Expenditure grew by R 34.97 m (11%) compared to FYE2015, amounting to R 347.04 m during the year.

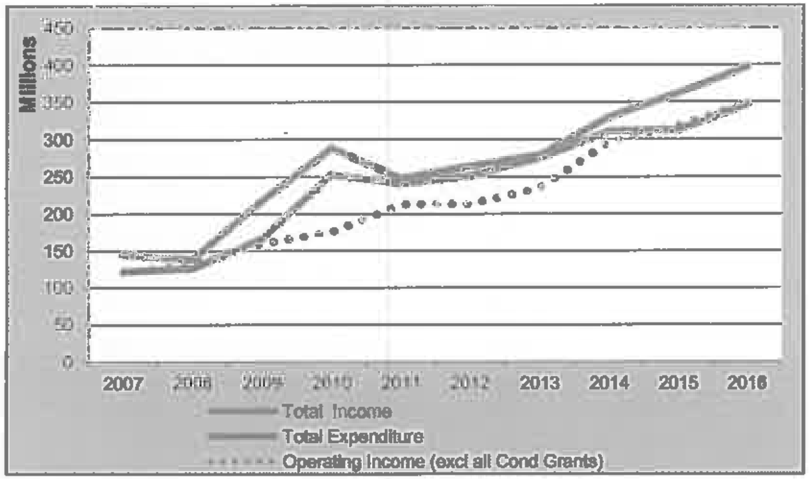
Salaries, Wages and Allowances increased by R 8.80 m (8%) to R 122.46 m in FYE2016. The Staff costs/total expenditure ratio of 35% is considered within the municipal norm of 25%-40% set by National Treasury.

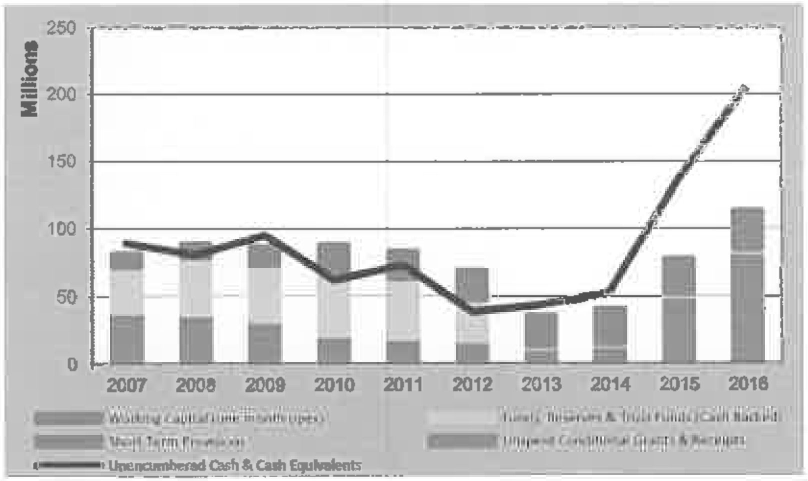
Expenses associated with **_Electricity Services_** increased by R 12.22 m (12%) and constituted 33% of Total Expenditure in FYE2016.

Repairs and maintenance grew by R 3.78 m (32%) in FYE2016 from R 11.91 m in the prior year, and amounts to 2.5% of carrying value of PPE, as opposed to the 8% recommended by National Treasury.

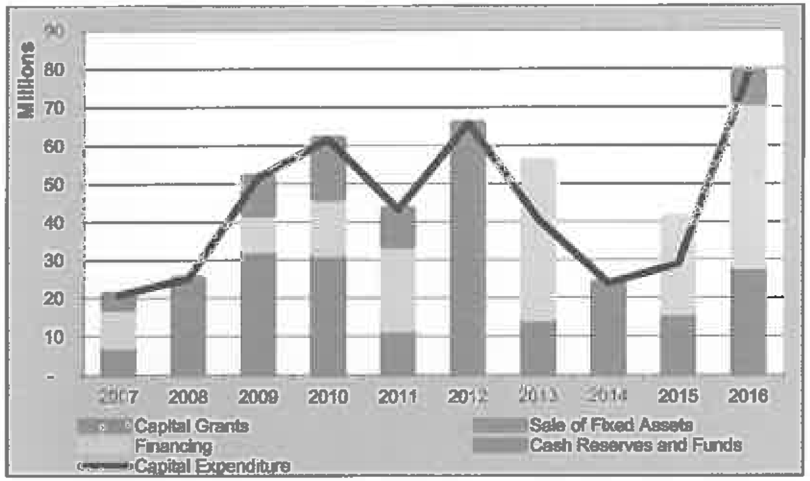
Cash Flow

Total Operating Income (excluding Capital Grants) continues to exceed ***Total Expenditure***. Operating Surplus decreased by R 12.48 million (36%) in FYE2016, amounting to R 22.36 million. The Municipality kept on posting a Cash Operating Surplus in the past three financial years which increased by R 5.63 million (8%) to R 77.65 million in FYE2016.





Capex increased significantly by R 49.81 million (173%) and amounted to R 78.68 in FYE2016 (FYE2015 – R 28.87 million) of which R 67.42 million was for infrastructure spend, funded from a variety of sources. ***External Financing*** remained the main funding source at R 43 million (55%), followed by ***Capital Grants*** of R 27.46 million (35%) and ***Cash Reserves and Funds*** of R 7.56 million (10%) during the same period.



Since 2013, ***Unencumbered Available Cash*** showed an increasing trend. It amounted to R 206.79 million and covers all statutory requirements as well as 1 month's working capital as at FYE2016. The municipality kept on posting a cash surplus above the minimum required liquidity since 2013. At FYE2016 the surplus amounted to R 104.79m, the highest in the ten year assessment period.

Unspent Conditional Grants increased by R 32.23 m (85%), while Short Term Provisions increased by 5% and amounted to R 6.45 m. These items as well as Reserves are fully cash backed and totalled R 78.48 m in FYE2016, an increase of 71% from the previous financial year end as depicted in the table below.

Minimum Liquidity Levels

MINIMUM LIQUIDITY LEVELS	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Unspent conditional grants	32.12	29.91	27.20	11.31	6.93	2.84	1.75	2.07	37.73	69.97
Short term provision	6.17	6.66	1.86	6.17	7.79	9.43	4.83	5.88	6.12	6.45
Funds, Reserves & trust funds (Cash Backed)	32.57	41.08	40.98	46.28	44.48	31.43	1.67	1.83	2.02	2.06
Total	**70.86**	**77.65**	**70.04**	**63.76**	**59.20**	**43.70**	**8.26**	**9.78**	**45.88**	**78.48**
Unencumbered Cash & Cash Equivalents[2]	88.34	79.89	94.41	60.90	72.12	38.06	43.25	52.58	136.70	206.79
Cash Coverage Ratio (excluding Working Capital)[3]	**1.25**	**1.03**	**1.35**	**0.96**	**1.22**	**0.87**	**5.24**	**5.38**	**2.98**	**2.63**
Working Capital Provision [1 month Opex]4	10.13	10.46	12.59	19.84	18.48	19.33	21.12	24.09	24.05	23.52
Cash Coverage Ratio (including Working Capital)[5]	**1.09**	**0.91**	**1.14**	**0.73**	**0.93**	**0.60**	**1.47**	**1.55**	**1.95**	**2.03**
Minimum Liquidity Required[6]	80.99	88.10	82.63	83.60	77.67	63.03	29.37	33.87	69.92	102.00
Cash Surplus/(Shortfall)[7]	**7.34**	**-8.21**	**11.78**	**-22.70**	**-5.55**	**-24.97**	**13.87**	**18.71**	**66.77**	**104.79**

The municipality has commenced with cash backing a landfill rehabilitation reserve, by allocating R16 million (or 25% of estimated costs) towards this reserve and intends to completely cash back this cost over a 4-year pericd. This reserve will be accounted for in future and included in the minimum required liquidity calculations.

[2] Unencumbered cash and cash equivalents = Total cash and cash equivalents-Ceded investments
[3] Cash Coverage Ratio (excl. Working Capital) = Unencumbered cash and cash equivalents/Total
[4] Total Expenditure less Non-Cash Items/12
[5] Unencumbered cash and cash equivalents/(Total + Working Capital provision)
[6] Total + Working Capital Provision
[7] Minimum liquidity required - Unencumbered cash and cash equivalents

OUTCOME OF THE INDEPENDENT FINANCIAL ASSESSMENT

Hessequa's liquidity ratio has improved substantially since FYE2014 and currently stands at 1.84:1. The improvement in liquidity ratio is mainly attributed to a 51% increase in Cash and Cash Equivalents (R 70.09 million) and constituted 83% of Current Assets.

The municipality reported a collection rate of 97%. The collection level remained constant compared to the previous year and is above the municipal norm of 95% set by National Treasury.

As at FYE2016, unspent conditional grants and receipts continue to increase and amounted to R 69.97 million, an increase of 85% from the previous financial year and constituted 50% of Current Liabilities. This was mainly due to late receipt of financial support to repair flood damage and the delay in awarding the work pursuant to a tender appeal.

Gross Consumer Debtors continues an increasing trend since FYE2011 and averaged a growth of 9% annually in the last five years. Provision for Bad Debts has also increased during the same period and amounted to R 24.57 million and more than covers debtors older than 90 days (117%) in FYE2016. The highest proportion of debtors' is held in electricity services (35%), water services (17%) and property rates (15%), and begs the question whether adequate credit control and debtors management is applied. Debtors older than 90 days continued to be dominant and constituted 44% of Consumer Debtors in FYE2016. Bad debts written off on rates and service debtors amounted to R 1.86 million in FYE2016 (R 1.98 million – FYE2015).

Salaries and Wages increased by 8% to R 122.46 million in FYE2016 and constitute 35% of Total Expenditure compared to 36% in the previous year. The Staff costs/total expenditure ratio of 35% is within the municipal norm of 25% - 40% set by National Treasury.

Important to note is that the Water and Electricity Services are derived from Segmented Income Statement for the year ended 30 June 2016, and not from the Statement of Financial Performance.

Over the past ten assessed years, Total Operating Income exceeded Total Expenditure. Operating Surpluses, however, decreased by R 12.48 million (36%), totalling R 22.36 million in FYE2016. Positive to note that the municipality kept on posting Cash Operating Surpluses in the past three financial years which increased by 8% to R 77.65 million in FYE2016.

The External Gearing has increased in the past three financial years and is currently at 35%. Gearing remained below the recommended norm of 40% however (National Treasury recommends a maximum of 45%).

The accumulation of Unencumbered Available Cash accelerated substantially - a trend that started in 2012/2013. Cash and cash equivalents amounted to R 206.79 million as at FYE2016 which represents a cash surplus above the minimum liquidity required to cover all statutory requirements including one month's working capital of R 104.79 million. This cash surplus is the highest in a ten year period.

Capital expenditure increased by R 49.81 million (173%) and amounted to R 78.68 in FYE2016 (FYE2015 – R 28.87 million). The funding mix consists of External Financing which remained the main funding source at R 43 million (55%), Capital Grants at R 27.46 million (35%) and Cash Reserves and Funds of R 7.56 million (10%) during the same period.

Net Cash from Operating Activities increased by R 18.83 million (19%) in FYE2016 from R 97.10 million in the previous year. Net Cash flow from investing Activities decreased by R 51.54 million (195%) from R 26.48 million in FYE2015 as a result of a large amount of R 78.68 million invested in capital expenditure. The municipality continues to improve its cash position, which amounted to R 206.79 million in FYE2016 from R 136.70 million in the previous year.

STRENGTHS

- Healthy and stable Liquidity Ratio;
- Stable payment ratio above the required norm;
- Acceleration of the accumulation of available cash;
- Sufficient provision is made to cover debtors older than 90 days;
- Posting of cash operating surplus in the past three years;
- Sufficient unencumbered available cash that covers all statutory requirements as well as 1 month's working capital with a Cash Coverage Ratio of 2x.

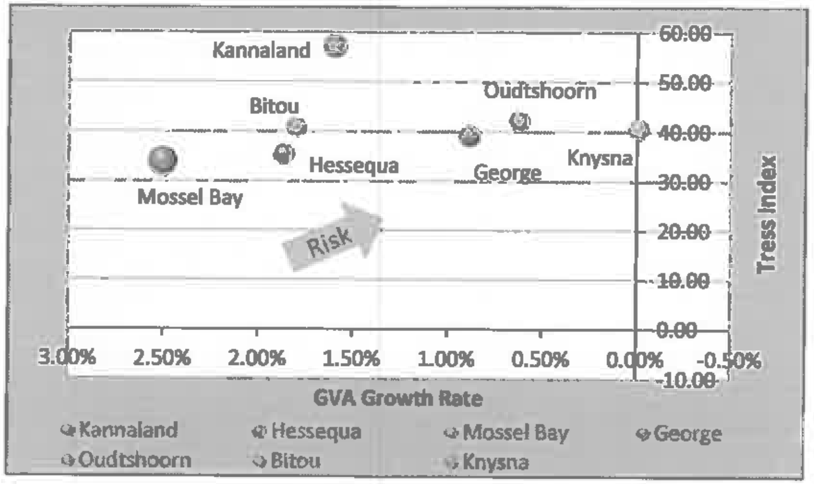
WEAKNESSES

- Continuous increase of unspent conditional grants;
- The continuous increase in gross consumer debtors, which requires a concerted effort at credit control and debtor management;
- Increasing trend of gearing level. At 35% it does not pose a problem currently but discretion needs to be exercised when borrowing in future.

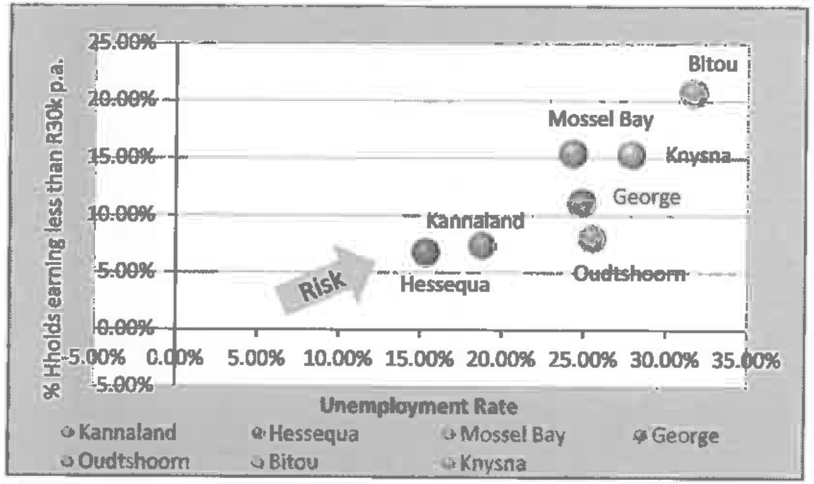
1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	**Future Revenues**
5	Affordable Future Capital Investment
6	Scenario Analysis
7	Ratio Analysis
8	Conclusions

MUNICIPAL REVENUE RISK INDICATOR (MRRI)

Hessequa has a R 2.1 billion economy (constant 2010 monetary terms). Its average economic growth rate during the past 5 years of 1.9% p.a. was the second highest in the district after Mossel Bay, higher than the average population growth rate of 1.3% p.a. for the same period. This resulted in an ***Economic Risk*** component of the MRRI for Hessequa of Medium.

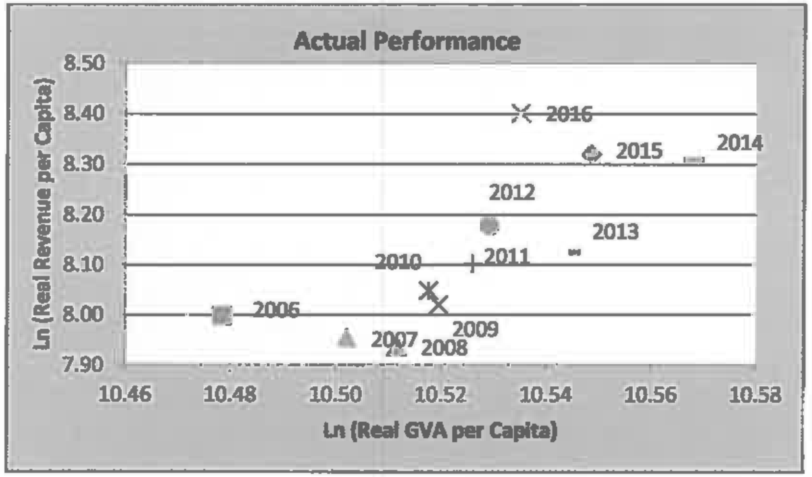


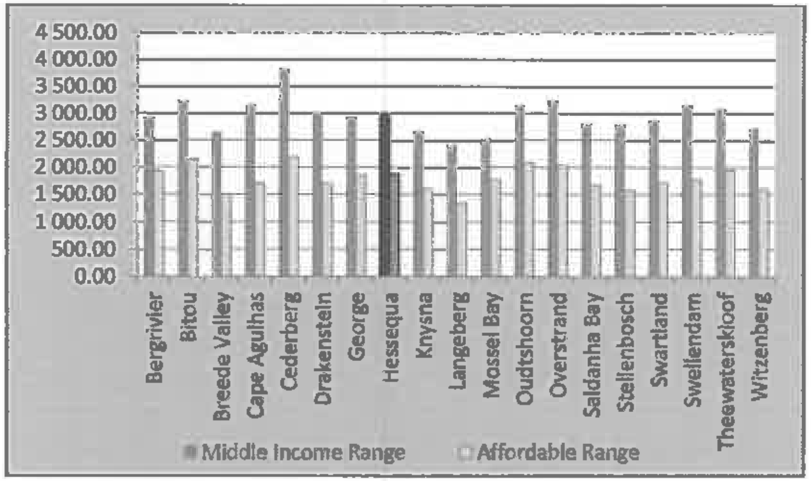
The unemployment rate of 15.3% and the percentage of households in Hessequa earning less than R30 000 p.a. of 6.8%, are the lowest relative to the other municipalities in the district. These factors combine to provide a moderate ***Household Ability to Pay Risk*** component of the MRRI.



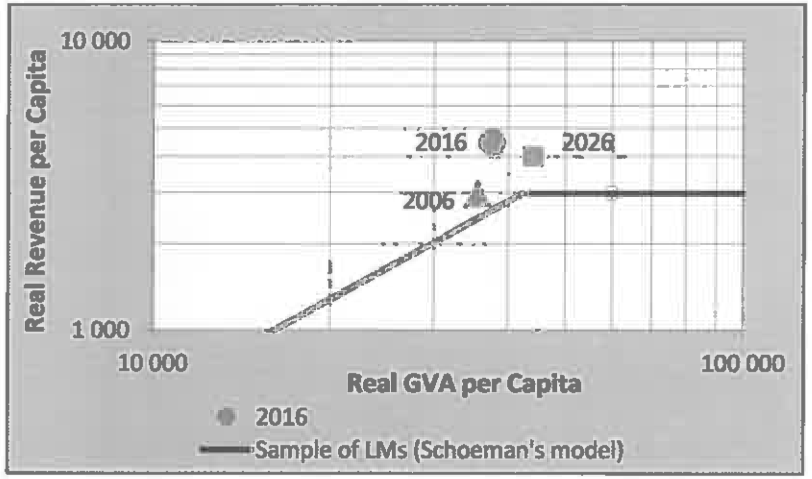
The Economic Risk and Household Ability to Pay Risk combine to a resultant Municipal Revenue Risk Indicator ("MRRI") of ***Medium.***

Between 2006 and 2008, an increase in the ***Real GVA per Capita*** resulted in a slight decrease in the ***Real Municipal Revenue per Capita***. Since then the Real Municipal Revenue per Capita increased albeit against a decline in Real GVA per Capita since 2014. The developments anticipated in Hessequa auger well for a further increase in the Real Municipal Revenue per Capita, but hopefully associated with a concomitant increase in Real GVA per Capita.





In 2006 and 2016 the ***Real Revenue per Capita*** exceeded the expected amount for the Real GVA per Capita as researched by Schoeman[8]. In real terms the projected revenue per capita in 2026 is less than the revenue per capita in 2016. This provides comfort in the light of the proportional growth of indigent households.

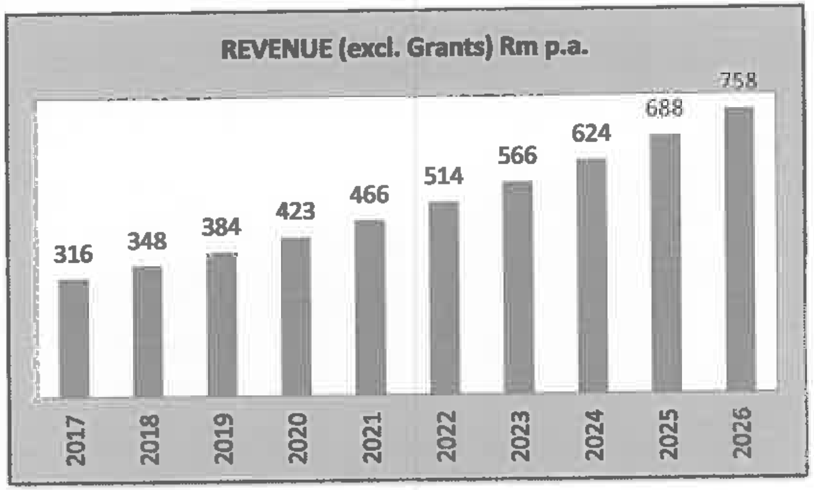


A comparison of the ***Average Household Bill*** for the Middle Income- and Affordable Ranges of a selected number of municipalities in the WC, based on the 2016/17 tariffs reveals that Hessequa features in the 2nd Quartile for both the Middle Income- and Affordable Ranges, i.e. slightly more than the average bill for these municipalities. This is an indication that the households in Hessequa are not overly burdened relative to other municipalities in the province.

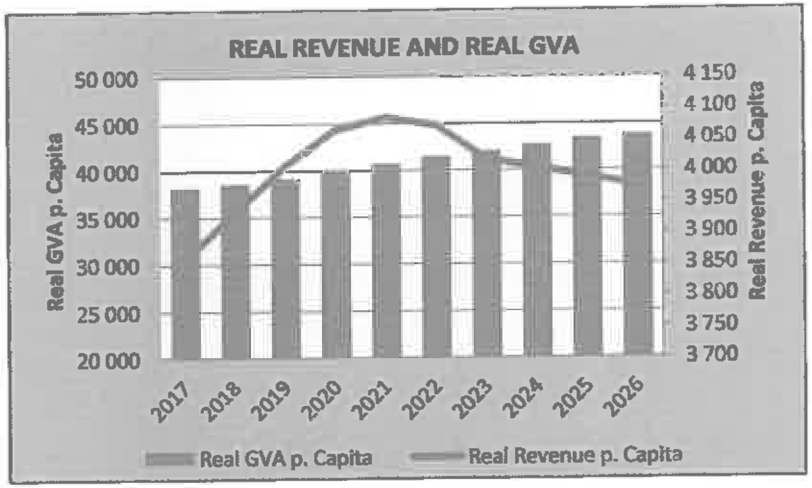
[8] *Fiscal Performance of Local Government in South Africa - an Empirical Analysis*; Niek Schoeman; UP 22 July 2011; https://editorialexpress.com/cgi-bin/conference/download.cgi?db_name=IIPF67&paper_id=40

It is estimated that approximately 2 500 new residential stands will be developed in Stilbaai during the next 10 years. These developments will have spinoffs in the economy due to upstream and downstream linkages that will impact on the revenue that the municipality is expected to generate. Due to the uncertainty of the rate of development, the expected future revenues only have a measure of probability of occurring.

Based on the development assumptions the ***Future Nominal Revenue*** (excluding Grants) is growing at an average rate of 9.6% p.a. This is a combination of (i) tariff increases (ii) increased sales and (iii) additional revenue sources.



Real ***GVA per Capita*** shows a gradual increase during the 10-year period, and the ***Real Revenue per Capita*** for the municipality ranges between R 3 800 and R 4 100 p.a.



1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	**Affordable Future Capital Investment**
6	Scenario Analysis
7	Ratio Analysis
8	Conclusions

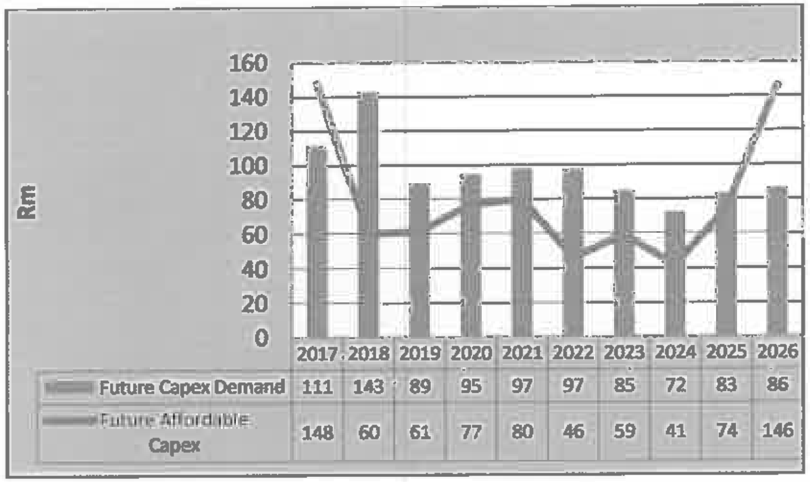
CAPEX AFFORDABILITY AND FUNDING

Total 10-year Capex Demand = R 958 million

Total 10-year Capex Affordability = R 791 million

The Capex Demand exceeds the Capex Affordability as illustrated in the Graph below. It needs to be stressed however that the capex demand estimates are now approximately 3 years old and need to be revisited.

Capex Affordability vs Demand



IPM's model accommodated the intended capex budget as reported in its MTREF Budget, however in an attempt to improve the gearing and liquidity, the external financing was extended over a period of 5 years from 2016/17 to 2020/21.

In the event that the MTREF capital funding mix were to be implemented in a prolonged absence of any significant structural revenue growth the gearing would increase to unacceptable high levels of 60% and the minimum required liquidity would be breached between 2021 and 2024 with a maximum liquidity gap of –R 19 million in 2022. The municipality will only have surplus cash available during the latter 2 years of the 10-year planning period to build up a cash backed Capital Replacement Reserve ("CRR").

For purposes of this report the minimum required liquidity level caters for unspent conditional grants, short term provisions, and 1 month working capital.

In the Revised Scenario in which the borrowings are extended over a period of 5 years and not the originally budgeted 3 years, and revenue and expenditure associated with an additional 2 500 stands in Stilbaai are included, albeit spread over a period from 2019 to 2025; then both the gearing as well as the liquidity improve.

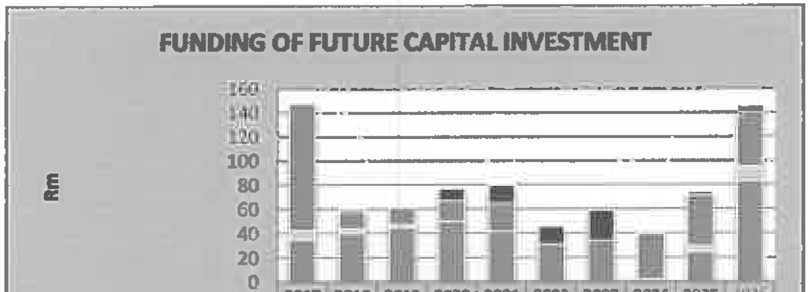
The capital funding mix for such a Revised Scenario is presented in the table below:

Funding Mix

10-YEAR ESTIMATED FUNDING SOURCES		
Source	**Base Case**	**%**
New Loans	R 319	40.4%
Own Cash	R 33	4.2%
Grants	R 361	45.7%
Other	R 78	9.8%
Total	**R 791**	**100.0%**

The capital contribution from private developers was estimated to amount to R 78 million and is included in "Other" sources of funding. In the Base Case almost 46% of capex funding is sourced from Grants. The availability of grants to serve a growing indigent population needs to be assessed in the face of the prevailing fiscal constraint.

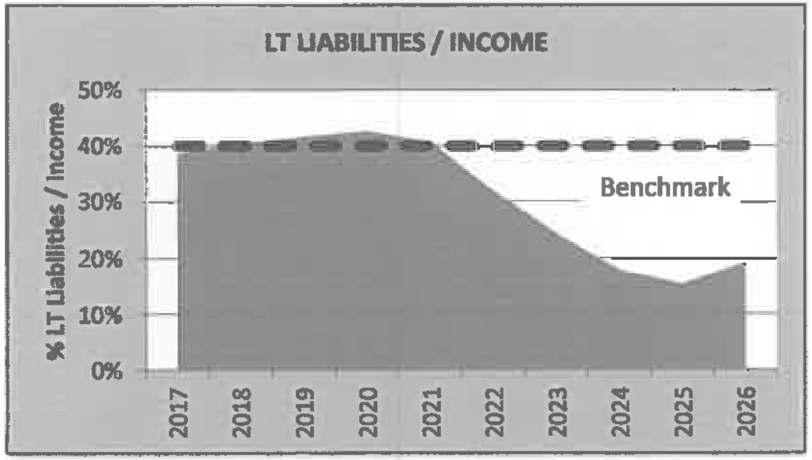
The distribution of the funding mix for IPM's revised Scenario is presented below:



	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Other Capital Contributions	0	3	0	10	15	15	25	2	3	5
Grants	105	13	14	17	23	31	34	37	41	45
Own Cash	8	4	2	0	0	0	0	2	5	12
New Loans	35	40	45	50	42	0	0	0	25	83
Existing Loans	0	0	0	0	0	0	0	0	0	0

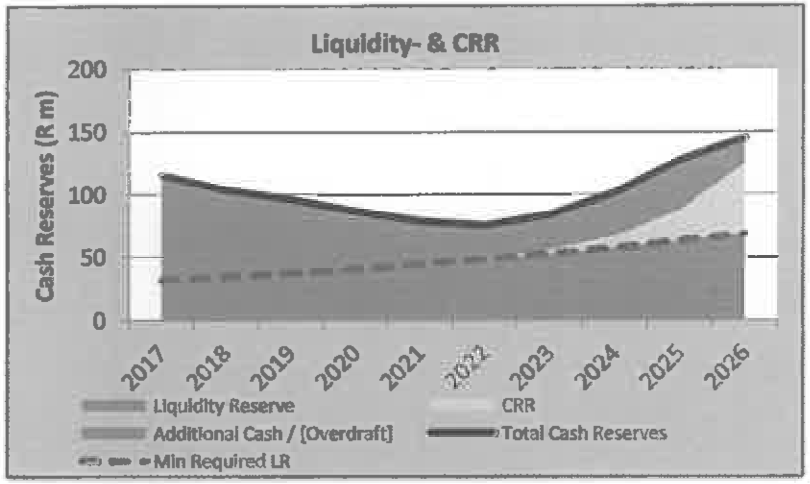
Gearing

Notwithstanding the fact that the MTREF borrowings are spread over 5 years, the gearing (Interest Bearing Liabilities / Total Income) is breached slightly, if 40% is accepted as the benchmark. The External Loan Liability Paid Coverage Ratio which should at least be 1:1 and preferably 2:1 is breached in 2018 to 2020 as indicated in the Ratio Table on page 27.



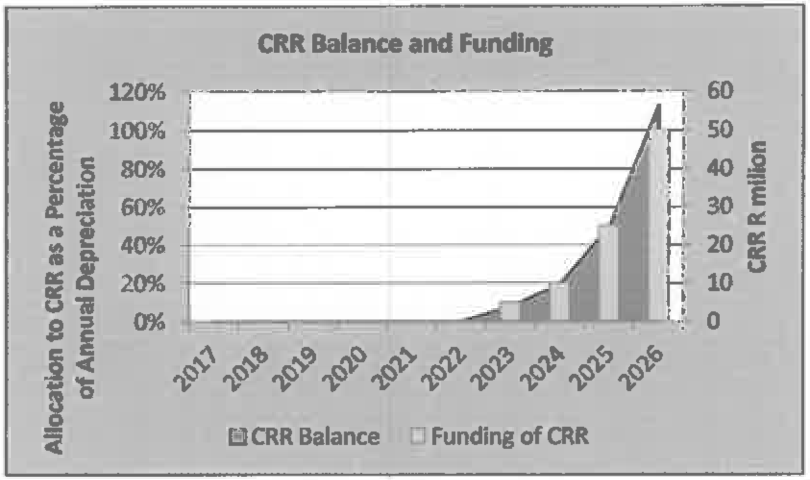
Liquidity

The municipality commences in July 2016 with a healthy balance of cash and cash equivalents. However due to the ambitious capital programme the cash balance reduces in future but in the Revised Scenario never breaches the minimum liquidity required.



Capital replacement Reserve ("CRR")

Whereas the available cash does not allow for the funding of a cash backed CRR during the initial years, the liquidity improves from 2023 onwards to allow a gradual increase in the allocation of cash towards such a fund. The premise is that available cash will be reserved in a dedicated CRR each year and that 50% of the balance of this reserve is used to fund capital expenditure.



1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	**Scenario Analysis**
7	Ratio Analysis
8	Conclusions

SCENARIOS

Realistic Upside and Downside Scenarios were compared to the Base Case Scenario.

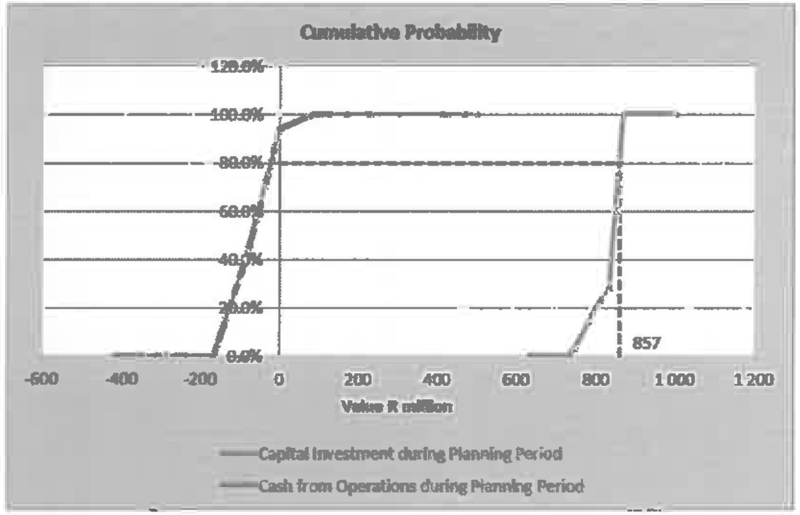
ASSUMPTIONS	BASE CASE	UPSIDE	DOWN-SIDE
Projected GVA Growth Rate p.a.	3.3%	3.8%	1.2%
Projected Population Growth Rate	2.4%	2.0%	2.8%
Year when structural change in salaries & wages is implemented	2018	2020	2020
Structural change in salaries and wages in 2020	0.0%	-1.0%	1.0%
Cost Factor of Salaries & Wages	1.0	1.00	1.05
Cost Factor on Electricity Services	1.0	1.00	1.05
Cost Factor on Water Services	1.0	0.95	1.00
Cost Factor on Repairs & Maintenance	1.0	1.00	1.00
Cost Factor on General Expenses	1.0	0.95	1.00
Collection Rate	95.7%	98.0%	94.0%

OUTCOME	BASE CASE	UPSIDE	DOWN-SIDE
Average annual % increase in Revenue	9.6%	9.2%	10.0%
Surplus accumulated during 10 years	372	581	74
10-year cash from operations after debt service	-66	89	-275
10-year LT Debt Raised	319	452	212
10-year capital investment programme	791	920	671
Cash investments after 10 years	145	351	-136

For the 10-year period, the Accumulated Surplus remains positive for all scenarios. Cash from Operations ranges between -R 275 m and R 89 m. The cash position after 10 years is a healthy R 351 m in the Upside but cash negative to the amount of -R 136 m in the Downside. The great variation of outcome for a realistic combination of input variables, demonstrates the need to manage the municipality's finances with care and discipline.

The probability outcome of a Monte Carlo Simulation on the 10-Year Cash after Debt Service and 10-Year Capital Investment Programme is illustrated below. There is a 80% probability that the Capital Programme will be less than app. R 857 million and almost a 100% probability that the cash generated after debt service will be negative.

Cumulative Probability Outcome of Monte Carlo Simulation



1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	**Ratio Analysis**
8	Conclusions

Predicted Ratios

The Base Case predicted ratios are presented below. Although the model is not programmed to measure the ratios as required by National Treasury in all instances, it does provide comfort that the municipality is sustainable in future - on condition that it operates within the assumed benchmarks set in the financial plan.

RATIO	HEALTHY NORM	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Liquidity Ratios											
Standard Liquidity Ratio	2 : 1	6.4 : 1	5.6 : 1	5.1 : 1	4.5 : 1	4.0 : 1	3.7 : 1	3.8 : 1	4.0 : 1	4.4 : 1	4.5 : 1
Quick Liquidity Ratio	2 : 1	4.9 : 1	4.1 : 1	3.6 : 1	3.0 : 1	2.5 : 1	2.2 : 1	2.2 : 1	2.5 : 1	2.8 : 1	2.9 : 1
Minimum Liquidity Level	1 : 1	4.5 : 1	3.7 : 1	3.2 : 1	2.6 : 1	2.2 : 1	1.9 : 1	2.0 : 1	2.2 : 1	2.6 : 1	2.7 : 1
Overdraft to Total Income	0	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Operational Ratios											
Accounting Surplus	>0	93	-4	1	12	26	38	61	54	69	80
Cash Operating Surplus	>0	-16	77	94	104	117	131	147	165	185	210
Repairs and Maintenance to Total Expenditure	7.0%	2%	2%	3%	3%	3%	3%	3%	4%	4%	5%
Consumer Collection Levels (incl. Fines)	>95%	85%	83%	83%	82%	82%	81%	81%	81%	81%	81%
Staff Costs	25% - 40%	38%	38%	38%	37%	37%	37%	37%	37%	37%	37%
External Gearing Ratios											
External Loan Liability Paid Coverage Ratio	2 : 1	3.8 : 1	0.8 : 1	0.8 : 1	0.9 : 1	1.1 : 1	1.4 : 1	2.0 : 1	1.9 : 1	2.3 : 1	2.0 : 1
External Interest and Capital Paid to Total Expenditure	7.5%	9%	9%	10%	11%	11%	9%	8%	7%	6%	8%
External Gearing Ratio	40.0%	38%	40%	42%	42%	40%	31%	24%	18%	15%	19%

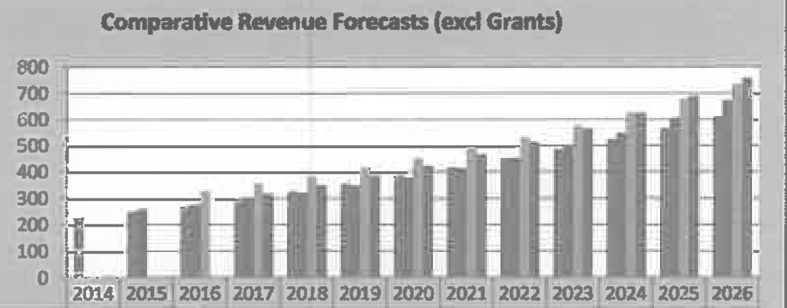
1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	Ratio Analysis
8	**Conclusions**

CONCLUSIONS

Revenues

The forecast Real Revenue per Capita exceeds the expected revenue per capita based on research done for municipalities with similar size economies and population sizes. Compared to a selection of municipalities in the Western Cape the household bill for a basket of services features in the 2nd quartile of those municipalities. The average economic growth rate for the past 5 years exceeded the population growth rate. The unemployment rate is moderate. These factors combine to produces a Municipal Revenue Risk Indicator (MRRI) of "Medium".

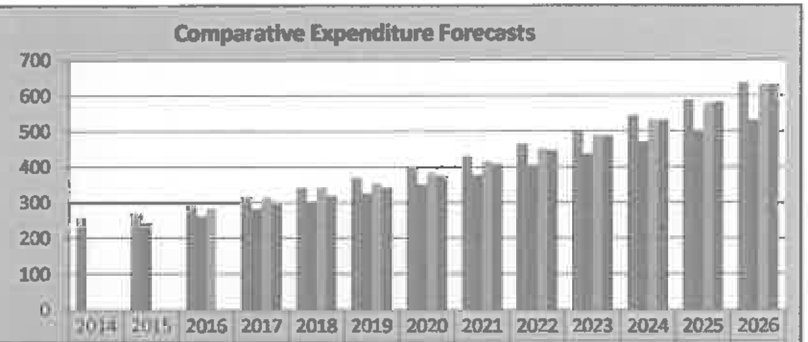
Due to the exceptional financial performance of the municipality recorded since the LTFP was first published in 2013, we have recalibrated our models. This resulted in revenue forecasts during the initial years that are comparable to the forecasts made in 2013 and 2014 but less than the forecasts of 2015. Due to the expected developments in the municipality that will result in a structural change of the economy, the revenue forecasts in the 2016 Estimate exceed those of the previous estimates in the later years.



	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
2013 Estimate	228	248	271	296	324	354	386	416	450	486	525	565	610
2014 Estimate		260	276	296	319	346	377	413	451	496	547	605	674
2015 Estimate			327	355	385	418	453	491	532	577	626	679	736
2016 Estimate				316	348	384	423	466	514	566	624	688	758

Expenditure

The expenditure pattern across the different years varies, but the latest 2016 Estimate is more or less on par with the previous estimates except for the 2014 Estimate, which is consistently lower. The additional developments envisaged will also impact on the expenditure patterns and we are comforted by the fact that the 2016 Estimate projects expenditure in 2026 that is on the higher end.



	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
2013 Estimate	260	270	292	316	341	369	399	431	466	504	544	589	636
2014 Estimate		243	261	280	302	325	350	376	405	436	469	500	532
2015 Estimate			283	313	342	353	383	415	451	490	532	579	631
2016 Estimate				294	318	341	373	407	446	487	532	581	632

Base Case

The Base Case Outcome for 2013, 2014, 2015 and 2016 estimates are compared in the table below:

Description	2013 Estimate	2014 Estimate	2015 Estimate	2016 Estimate
Average annual % increase in Revenue	8.6%	8.4%	9.7%	9.6%
Surplus accumulated during 10 years Rm	215	474	234	372
10-year cash from operations after debt service Rm	24	350	196	-66
10-year LT Debt Raised Rm	249	258	420	319
10-year capital investment programme Rm	632	662	888	791
Cash investments after 10 years Rm	44	99	155	145

The 10-year periods for the different estimates differ and it is difficult to make direct comparisons.

Comparatively speaking the 2015 Estimate would appear to be on the optimistic side. Due to the incremental adjustments made each year on the model based on the latest financial, demographic and economic information we always place more reliance on the latest outcome, i.e. 2016 Estimate. In all instances the Cash Position at the end of the 10-year period is positive.

Funding Sources

It is estimated, based on the experience to date that the proportional reliance on Capital Grants will dominate (46%). We have in the latest estimate also included an amount of developers' capital contributions (R 78 m) under "Other" Sources. The improved financial position and creditworthiness of the municipality allows it to borrow R 319m in the 2016 Estimate, and safeguard its liquidity by using less own cash resources for capex.

Source of Funding	2013 Estimate Rm		2014 Estimate Rm		2015 Estimate Rm		2016 Estimate Rm	
New Loans	249	39%	258	39%	420	47%	319	40%
Own Cash	37	6%	261	39%	220	25%	33	4%
Grants	346	55%	144	22%	246	28%	361	46%
Other	0	0%	0	0%	3	0%	78	10%
TOTAL	632	100%	663	100%	888	100%	791	100%

Note: The 10-Year periods differ for the three Estimates and can only provide an indication of changes among them. The 2015 Estimate appears to be overly optimistic.

Review of Recommendations made in 2013

Refer to p. 41 – 43 of the *Hessequa Local Municipality Long Term Financial Plan: 2014 – 2023*; October 2013

NO.	RECOMMENDATION	COMMENT
1	Increase Municipal Revenues	Remains Relevant. It is estimated that the new developments in Stilbaai in the next 10 years will contribute towards an average revenue growth rate of 9.6% p.a.
2	Sell investment Property	The improved financial situation makes this recommendation less essential.
3	Manage expenses	Cost control during the past year was exemplary but the recommendation remains relevant
4	Maintain Liquidity Reserve	Liquidity has improved significantly, but the recommendation remains relevant.
5	Downward Adjustment of Salaries and Wages Bill	The average percentage employee related expenses to total expenditure (37%) is within the benchmark proposed by National Treasury (40%). The recommendation remains relevant however and needs to be monitored closely. Prudency is required in making new appointments.
6	Support to indigents	Remains relevant. Optimise service levels within available funds.
7	Prioritise capital investment programme	The estimated capex demand still exceeds the affordability. The recommendation remains relevant. The capex demand (new and replacement capex) was determined during the preparation of the LTFP in 2013 and needs to be revisited.
8	Assess condition of assets accurately	Remains relevant to ensure timeous replacement.
9	Migrate asset register to become a decision-making tool.	Remains relevant.
10	Debt affordability	Adjusted to R 319m for the planning period.
11	Recommendations emanating from discussion with Executive Management.	All recommendations remain relevant to the extent not yet achieved.
12	***New Recommendations added in the 2015 Estimate:***	
13	Align external fund raising to capex programme	Ensure that future borrowings are aligned to the expected capital spending pattern. This recommendation remains valid but borrowings also need to be phased to ensure that gearing and liquidity criteria are met.
14	Cash back a Capital Replacement Reserve ("CRR")	The cash surplus generated is not sufficient to cash back the depreciation charge in a CRR, but the 2016 Estimate determines that municipality should be able to start funding a CRR from 2023 onwards.
15	Adjust R&M budget upwards.	Continuously increase the R&M budget to reach the proposed 8% of Carrying Value of assets to ensure the health of existing assets. This recommendation remains valid

Concluding Remarks

1. The municipality has demonstrated the ability to post operating cash surpluses.
2. The municipality improved its liquidity as evidenced by a Current (Liquidity) Ratio of 1.8 :1 and a strong Cash Cover Ratio of 2.0x.
3. The period of consolidation of capital expenditure has made way for accelerated investment in capital assets during the past 3 years.
4. Gearing has increased to 35% in FYE2016 inviting caution when borrowing in future.
5. The municipality continued to maintain a high (97% - annual average) Revenue Collection Level.
6. The environment within which the municipality operates exhibits a "Medium" risk to generate own revenue. Whereas revenue generation per capita in real terms is high, the household bill for services delivered by the municipality is of an average amount. This calls for a judicious tariff setting policy and accelerated local economic development.
7. We estimate that the municipality will be able to invest in a capital programme of R 791 million in the planning period to FYE2026 and be able to afford that 40% of this capex is funded with external financing.
8. The municipality's 3-year MTREF capital budget is optimistic and the budgeted funding mix will result in the breach of gearing and liquidity criteria. We have consequently prepared a Revised Scenario in which the borrowing budgeted for the 3-year MTREF period is extended over a 5-year period.
9. The Scenario analysis indicates that a great variation of outcome for a realistic combination of input variables is possible and demonstrates the need to manage the municipality's finances with care and discipline.

PROJECTED STATEMENTS

STATEMENT OF FINANCIAL PERFORMANCE	1	2	3	4	5	6	7	8	9	10
R '000 000	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Revenue										
Property rates	69.91	75.18	80.84	89.10	98.25	109.33	120.54	132.92	146.61	159.16
Operational Grants Recognised	48.47	48.95	52.65	56.55	60.79	65.41	70.45	75.94	81.94	88.50
Income electricity services	127.04	139.03	152.02	167.55	184.75	205.59	226.67	249.96	275.69	299.28
Income water services	29.31	31.47	33.78	37.23	41.05	45.68	50.37	55.54	61.26	66.50
Agency Services	1.90	2.02	2.16	2.31	2.47	2.65	2.84	3.04	3.27	3.51
Other service charges and income	87.93	100.65	115.10	126.91	139.76	150.62	165.91	182.67	201.02	229.62
Total Revenue	**364.56**	**397.30**	**436.56**	**479.64**	**527.07**	**579.28**	**636.77**	**700.08**	**769.79**	**846.57**
Expenditure										
Salaries, wages and allowances	-148.44	-158.54	-170.98	-186.18	-201.38	-218.37	-236.66	-256.42	-277.76	-302.08
Expenditure electricity services	-86.46	-95.41	-104.38	-115.05	-126.70	-140.80	-155.23	-171.16	-188.77	-205.30
Expenditure water services	-6.91	-7.41	-7.93	-8.73	-9.61	-10.69	-11.79	-13.01	-14.35	-15.61
Repairs and maintenance	-16.51	-19.54	-21.67	-23.63	-25.80	-27.97	-30.31	-32.84	-35.58	-38.69
General expenses	-36.07	-37.52	-35.75	-39.87	-43.94	-48.43	-53.34	-58.77	-64.75	-70.42
Total Expenditure	**-294.39**	**-318.41**	**-340.70**	**-373.46**	**-407.43**	**-446.28**	**-487.34**	**-532.20**	**-581.22**	**-632.10**
EBITDA	70.17	78.89	95.87	106.19	119.64	133.02	149.43	167.88	188.58	214.47
Interest on Long Term Debt	-16.53	-19.27	-22.33	-25.48	-27.28	-24.01	-20.78	-17.54	-17.12	-23.57
Interest BB/[OD]	11.58	4.79	4.03	3.50	2.79	2.12	1.71	1.73	2.22	2.59
Depreciation	-31.33	-32.46	-33.59	-35.31	-37.07	-37.41	-38.27	-38.39	-39.80	-43.99
Surplus/Deficit	**33.89**	**31.95**	**43.98**	**48.90**	**58.08**	**73.72**	**92.09**	**113.68**	**133.88**	**149.50**

STATEMENT OF FINANCIAL POSITION	1	2	3	4	5	6	7	8	9	10
R '000 000	30-Jun-17	30-Jun-18	30-Jun-19	30-Jun-20	30-Jun-21	30-Jun-22	30-Jun-23	30-Jun-24	30-Jun-25	30-Jun-26
Current Assets										
Receivables	38.76	42.24	46.42	51.00	56.04	61.59	67.70	74.43	81.85	90.01
Investment for Liquidity	31.54	34.15	36.68	40.15	43.79	47.92	52.33	57.16	62.45	68.02
Investment for CRR	0.00	0.00	0.00	0.00	0.00	0.00	3.83	9.59	24.69	56.34
Other Encumbered Investments	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Cash in Bank	83.96	69.46	59.30	46.43	34.78	27.51	27.39	34.68	39.90	20.80
Non-Current Assets										
Property Plant & Equipment	760.19	787.58	815.13	856.75	899.50	907.92	928.63	931.60	965.69	1 067.49
Investment Property	51.38	51.38	51.38	51.38	51.38	51.38	51 38	51.38	51.38	51.38
Total Assets	**965.83**	**984.82**	**1 008.90**	**1 045.70**	**1 085.49**	**1 096.31**	**1 131.26**	**1 158.84**	**1 225.96**	**1 354.04**
Current Liabilities										
Creditors	24.20	26.17	28.00	30.70	33.49	36.68	40.06	43.74	47.77	51.95
Bank Overdraft	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
ST Non-Interest Bearing Liabilities	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Non-Current Liabilities										
LT Interest Bearing Liabilities	140.10	160.83	181.88	204.10	215.01	184.82	155.23	124.93	118.73	162.44
LT Non-Interest Bearing Liabilities	46.68	50.74	55.20	60.12	65.53	71.49	78.07	85.33	93.35	102.22
Accumulated Surplus & Reserves	754.85	747.08	743.82	750.80	771.46	803.32	857.90	904.84	966.11	1 037.43
Total Liabilities	**965.83**	**984.82**	**1 008.90**	**1 045.70**	**1 085.49**	**1 096.31**	**1 131.26**	**1 158.84**	**1 225.96**	**1 354.04**

CASH FLOW STATEMENT	1	2	3	4	5	6	7	8	9	10
R '000 000	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Cash In										
Surplus / [Deficit]	33.89	31.95	43.98	48.90	58.08	73.72	92.09	113.68	133.88	149.50
Add Depreciation	31.33	32.46	33.59	35.31	37.07	37.41	38.27	38.39	39.80	43.99
Deduct Impairment	-45.68	-51.39	-56.51	-63.94	-70.31	-81.73	-89.91	-98.93	-108.86	-119.80
Proceeds from Sale of Assets	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Capital Grants	105.07	13.23	13.73	16.92	23.31	30.83	33.98	37.45	41.27	45.48
Other Capital Contributions	0.10	2.50	0.00	10.00	15.00	15.00	25.00	2.00	3.00	5.00
LT Debt Raised	35.00	40.00	45.00	50.00	41.50	0.00	0.00	0.00	24.82	82.96
Total Cash In	**159.70**	**68.74**	**79.80**	**97.20**	**104.65**	**75.23**	**99.43**	**92.58**	**133.91**	**207.14**
Cash Out										
Invest in PPE	-147.70	-59.85	-61.14	-76.92	-79.82	-45.83	-58.98	-41.36	-73.88	-145.79
Invest in Cash Backed Reserves	-31.54	-2.61	-2.53	-3.47	-3.64	-4.13	-8.24	-10.59	-20.39	-37.22
Working Capital	-86.53	-1.51	-2.34	-1.89	-2.25	-2.36	-2.74	-3.04	-3.38	-3.98
LT Debt Repaid	-16.76	-19.27	-23.96	-27.78	-30.59	-30.18	-29.59	-30.30	-31.02	-39.26
Total Cash Out	**-282.52**	**-83.24**	**-89.96**	**-110.06**	**-116.30**	**-82.51**	**-99.54**	**-85.30**	**-128.68**	**-226.24**

Thank you

Tel: +27 [0]11 202 2210
Fax: +27 [0]11 202 2231

Unit F14, Pinewood Square
Pinewood Office Park
33 Riley Road
Woodmead